



**BREXIT PERSPECTIVE**

# Deal or no deal?

20 July 2017

The first substantial week of negotiations between the UK and the EU on Brexit concluded today. But is anyone any clearer as to whether a deal can be reached, and what the details of such an agreement would look like? Most people would answer with a ‘no’.

Deal, no deal or what kind of deal? These are fundamental questions, and as the Brexit process unfolds, there is a growing realisation of the enormity of the task at hand. A bit like peeling an onion; remove one layer only to find another one waiting underneath revealing yet another layer of complexity.

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Given the wide range of policy issues to be settled, the incredibly tight timescale, and the political uncertainty in the UK, prospects of a successful outcome are far from certain.

While politicians and officials got down to the details of negotiations this week, businesses are increasingly grappling with their own response to such an unprecedented scenario, and the impact on their business and investment plans.

Brexit has now hit the boardroom, and given the vacuum of information about the future regulatory environment in Europe, corporations are increasingly taking no-regret decisions to help future proof their business.

At the end of the first substantive week of negotiations our teams provide an update from Brussels and London.

## NEWS FROM THE BRUSSELS BUBBLE

The hotels and restaurants of Brussels hoped for a welcome boost this week as 98 British civil servants descended on the city for the second round of Brexit negotiations with the European Commission.

These officials will get to know the city well over the next 18 months as they conduct monthly talks with their European counterparts to agree the details of Brexit. How much free time they'll have to enjoy the delights of the EU capital – and boost the profits of hoteliers – is another question.

If the first round in June was about the organisation of the negotiations, this week was about the presentation of each side's respective positions. As Michel Barnier, the EU's chief negotiator, mentioned at today's closing press conference: 'we make better progress when our respective positions are clear'. The third round, later in August, will seek to confirm what they can agree on and conversely to clarify the reasons for those areas of divergence. As both sides acknowledged – the clock is ticking.

### Format of the negotiations

The negotiation rounds are now structured on a monthly basis with several working groups tackling what is now commonly referred to as the 'divorce' proceedings. The EU has been insistent on following a two stage process. Any agreement on the future trade relationship will only start once satisfactory progress has been made on an orderly UK withdrawal.

Barnier confirmed that the approach his team is taking in the talks is one based on unity; the agreed approach of the other 27 Member States of the EU. A former French foreign minister and European Commissioner, his media profile has been rising exponentially, and his appearances are one of the hottest tickets in town. So far he appears to be suavely managing the infamously fractious and territorial Brussels audiences well.

## Issues at play

Three negotiating groups have been established, namely on citizenship issues, the financial settlement (the 'divorce bill'), and other so-called 'separation' issues. A separate group has also been set up to work on the Ireland/Northern Ireland border issue.

Much of the talks have been based on position papers that have now been published by both sides. During the meetings, these are then discussed and interrogated as both sides try to understand their respective positions, differences, and potential routes through.

So where are the two sides more closely positioned?

Barnier also emphasised today that progress had been made with regards to the issues of the rights of EU and British citizens post-Brexit. That both sides have already published detailed position papers had allowed the negotiators to make progress by clearly providing the level of clarity they need to move the negotiations forward. The 'fundamental' sticking point is who will have jurisdiction on defending their respective rights.

The European Parliament meanwhile – which will have to approve the final Brexit deal – has already put its cards on the table dismissing the UK's initial offer on citizenship as falling short of its own ambitions to put citizens first, according to Guy Verhofstadt, its Brexit coordinator. Improve the offer to EU citizens or we'll veto the deal, he went on to say earlier this month. Barnier also pointed to a shared commitment to the difficult and technical issues related to the Irish border.

More divergence than convergence could be seen on the politically-charged issue of the financial liabilities of the UK and EU. Barnier was clearly more negative on this thorny issue. An orderly withdrawal means accounts must be settled, he said. The UK needs to clarify its position. The EU is demanding a potential settlement from the UK which could amount to tens of billions of euros to cover its residual commitments after it leaves the bloc; clearly an extremely sensitive issue for the UK government. Barnier emphasised that progress on this issue was a key component of the wider 'divorce' settlement. Without

progress the EU-27 will be reluctant to allow the second stage around trade.

There is clearly not enough evidence yet that the talks are progressing in the right way. Each stage unveils the enormity of the task at hand and the realisation that some sort of transition period will be needed to manage the volume of work that realistically needs to be done to avoid the dreaded cliff edge scenario. Tick tock.

## A question of unity

The unity of the Commission and the EU-27 has been a striking feature of the talks to date. This is understandable given their joint interest in agreeing a financial settlement, certainty for their citizens, and the political imperative of Ireland.

But it is not a given that such a position will last the negotiations. Despite the current shared interest, political and national priorities are at risk of coming to the fore, dislodging the unity argument. The EU faces some tough issues over the coming months which could risk the shared positions that they currently hold. Brexit is not the only meal on the menu. These other issues include a potential rupture in relations between the EU and Poland over the latter's constitutional reforms; discussions over the future shape of the EU's long term budget once the UK leaves and the threats of a separatist referendum in Catalonia. Any one of these could force a break. A triumphant Merkel in September could also reignite the Franco-German engine alongside her new best friend Emmanuel Macron, potentially ruffling feathers if it starts to dominate the unity approach.

## Outside Brussels

The negotiations are not taking place in a vacuum. In the real world, businesses continue to take investment decisions about what the future regulatory environment will be. Unlike the UK, we haven't yet seen European business take a significantly vocal stance. But this could change if progress is not made as swiftly and smoothly as

needed. Political and regulatory uncertainty is not good for business and investment decisions cannot be put on hold indefinitely. The European agriculture sector is starting to get jittery, particularly from the Irish. The Flemish Government has already called for a soft-Brexit. We are seeing the drip feed of announcements about UK based businesses hedging their bets by relocating some staff to new EU locations with the financial services and airline industry particularly prominent.

All in all, as the process of disentangling the UK from the EU continues, it becomes more evident that there is much to be done. Deal or no deal it's 'time to get down to business'. As Barnier concluded: 'we know we have to compromise. We are not there yet. We need clarity.' Let's see what August brings.

## LONDON CALLING....

On one side of the table, Michel Barnier sits with a stack of notes. On the other, David Davis sits with a notable absence of paperwork. Monday marked day one of the first substantive round of Brexit negotiations following preliminary talks, with the scene at the EU's headquarters viewed as a metaphor for how UK negotiations are currently seen by many commentators: uncoordinated and ill-prepared. It is easy to overstate such presentational issues – it merely reflects different ways of working.

Nicky Morgan said the UK would not achieve a 'pain-free Brexit'. The newly-elected chair of the influential Treasury Select Committee, a frequent critic of the Prime Minister's Brexit strategy, is now well positioned to campaign for the government to take her preferred softer Brexit. This comes after a weekend of Cabinet infighting, with senior ministers briefing against each other in a demonstration of the "chaos" May predicted if Labour came into power. Making matters worse, the Chancellor, Philip Hammond, has suggested the UK continue to draw funds from the European Investment Bank to fund its infrastructure projects, and is warning against leaving the EU without any deal, a significant chasm between the Prime Minister's 'no deal is better than a bad deal' view.

Davis, meanwhile, the UK's chief Brexit negotiator, quickly returned to London on Monday to vote in a three-line whip on time allocated to backbenchers' legislation. Eyebrows are being raised over how much attention a minority government, vulnerable to rebellion, can give to Brexit. This is also further illustration of Parliament's emboldened role: May must seek considerable consensus if her plans are to move forward.

On Thursday, Davis returned to Brussels for a further round of talks. Holding a press conference with Barnier shortly afterward, Davis reiterated the government's view that it has responsibilities, but added the UK has rights, too. There were moments of divergence: Barnier continued to insist on ECJ jurisdiction for EU citizens post Brexit. Davis maintained that following the discussions, there is "a lot to be positive about", despite Barnier stating that negotiations will not progress until the UK clarifies its policy positions.

The government wants to portray that it has the UK's departure from the EU under control. This is important from a negotiation standpoint, as well as reassuring an increasingly uncertain business community. The Repeal Bill still intends to abrogate the European Communities Act 1972, but it is no longer prefixed by "Great". The UK government will want to keep on side the 30 or so Tory MPs who are vehemently pro-Europe.

All this makes for plenty of negative media coverage for Theresa May. Her only consolation will be that Labour is equally unprepared for Brexit talks. A poll released this week shows that 80% of the party's members oppose Jeremy Corbyn's intention to withdraw from the Single Market.

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